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C O N F I D E N T I A L SECTION 01 OF 03 ALMATY 000869

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FOR SECRETARY BODMAN FROM AMBASSADOR ORDWAY

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TAGS: [ENRG](#) [EPET](#) [OVIP](#) [KZ](#)

SUBJECT: SCENESETTER FOR SECRETARY BODMAN'S VISIT TO
KAZAKHSTAN

Classified By: Amb. John Ordway, reasons 1.4 (B) and (D).

¶1. (C) Summary: Embassy Almaty welcomes your upcoming visit to Kazakhstan. We wanted to use this occasion to provide you with background on some of the most important energy and nonproliferation issues where your engagement with the Government of Kazakhstan (GOK) could help us move forward. Oil and gas transportation issues are critical to landlocked Kazakhstan. The GOK is currently engaged in two sets of pipeline negotiations -- with the Azeris to secure access of Kazakhstani oil to the BTC pipeline, and with Russia and consortium partners to expand the CPC pipeline -- which have either stalled or are deadlocked. You might use your conversations with GOK officials to solicit their views on how to move these negotiations forward. We also have a keen interest in moving Central Asian gas to market. One proposal for doing so is building a Trans-Caspian gas pipeline from Kazakhstan to Azerbaijan; a joint agreement for a U.S.-sponsored feasibility study of the project might be a useful deliverable for a Nazarbayev visit to Washington.

¶2. (C) Summary (continued): We would also appreciate your advocacy to help secure ConocoPhillips' bid to develop the offshore "N Block" in partnership with the national oil and gas company, and to help resolve a long-standing legal case against an American citizen oil executive. During her recent visit to Kazakhstan, Secretary Rice encouraged increased infrastructure ties between Central and South Asian countries. We would appreciate your exploring this issue, and in particular the possibility of expanding electricity trade in the region, with your interlocutors. Finally, we hope that your meetings with the GOK will provide an opportunity to highlight our excellent record of non-proliferation cooperation with Kazakhstan, dispel any misperceptions about the BN-350 program, and obtain clarity on the GOK's views regarding the Second Line of Defense program.

Post-Election Overview

¶3. (C) President Nazarbayev officially won 91% of the vote in December's presidential elections. Notwithstanding the OSCE's determination that the election did not meet international standards, as well as the skepticism of the opposition and others about the official margin of victory, no one questions that Nazarbayev's was a landslide victory; a USG-financed exit poll showed the President getting 83% of the vote. Nazarbayev's popularity is based in large part on Kazakhstan's rapid economic expansion (9% GDP growth, 2002-2005) and political stability. Nazarbayev appears to have a mandate to build upon his economic successes, which include excellent macro-economic reform and successful

management of the country's oil revenues. In his annual "Address to the Nation" on March 1, Nazarbayev revealed an ambitious plan for further transformation of the economy, outlining various microeconomic reforms, reiterating Kazakhstan's ambition to join the WTO in 2007, and stressing the need to diversify the economy away from its dependence on the extractive industries.

14. (C) In terms of political reform, Nazarbayev is much more cautious. The February 11 murder of opposition leader Altynbek Sarsenbaiuly has clearly unsettled presidential insiders. Although none of the evidence gathered so far in the FBI-assisted investigation points toward either a political motive or the involvement of presidential insiders, rumors of both persist, and the President may be concerned by the possibility that the crime was engineered to destabilize his regime.

15. (C) Looking outward, Nazarbayev has long played an artful balancing act among Russia, China, and the U.S. Visits like yours -- along with the invitation he hopes to receive this spring to the Oval Office -- are important to him as a means of counter-balancing Russia and China's enormous gravity. Nazarbayev speaks often of increasing Kazakhstan's stature in the world community. In concrete terms, Kazakhstan is bidding for the OSCE Chairmanship in 2009; we are quietly encouraging them to delay until 2011, conditioning our support on further political reform. The U.S. - Kazakhstan relationship, though underpinned by our energy interests, is broad and deep. Kazakhstan is an ally in the War on Terror, maintaining a 29-member ordnance disposal contingent in Iraq and allowing no-cost overflights for Operation Enduring Freedom in Afghanistan. We enjoy excellent, and growing cooperation with Kazakhstan's intelligence agencies. And Kazakhstan's non-proliferation accomplishments make it a

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"success story" among post-Soviet States.

Oil and Gas Transportation Issues

16. (C) You are likely familiar with Kazakhstan's oil wealth: reserves are estimated at 40 billion barrels. From its current production of 1.2 million bpd (1 million of which is exported), Kazakhstan's output is projected to reach world top-ten levels, at 3.5 million bpd, by 2015. However, as a landlocked country far from world markets, Kazakhstan is critically dependent on pipelines to deliver its oil to market. Currently the bulk of Kazakhstani crude is exported via Russia, both through the Transneft system and the independent Caspian Pipeline Consortium (CPC) pipeline. Kazakhstan's ability to get its increased volumes of crude to market will depend, in the near future, on (a) CPC expansion and (b) successful negotiations to secure access of Kazakhstani oil to the BTC pipeline.

17. (C) Both set of negotiations have stalled. Russia is playing hardball in the CPC expansion negotiations, demanding favorable fiscal terms and, recently, adding the condition that CPC expansion be linked to the construction of a Burgos-Alexandroupolis (Bosphorus bypass) pipeline. The BTC negotiations appeared near completion in September, when the GOK and the Azeris initialed the Inter-Governmental Agreement (IGA). However, since September little progress has been made, and we now hear that the Azeris are considering re-opening key agreed-upon parts of the IGA. In neither of these cases do we perceive that the GOK is the fundamental obstacle to concluding negotiations. It would be very useful, however, to hear your interlocutors' views on how to unblock the current stalemates.

18. (C) Finally, though Kazakhstan has sizable gas reserves (3 bcms proven), it currently exports very little gas, serving principally as a transit country for Turkmenistan's and Uzbekistan's gas. The GOK has an ambitious plan, however,

for increasing gas production, both for export and for developing a local petrochemical industry. (Western oil companies view a Kazakhstani petrochemical industry as largely uneconomic, due to distance from market.) You may wish to use your visit to gauge GOK interest in a Trans-Caspian Gas Pipeline, running from Kazakhstan to Azerbaijan. While the GOK is also studying the possibility of a gas pipeline in China, only a Western route would deliver Kazakhstani gas to world markets. A joint agreement for a U.S.-sponsored feasibility study might be a useful deliverable for a Nazarbayev visit to Washington, giving the project greater political cover against near-inevitable strong Russian opposition.

Opportunities for Advocacy

¶9. (C) ConocoPhillips (CP) is currently in the last stages of a bid competition (against Shell) to partner with the state-owned oil company Kazmunaigaz (KMG) in developing the offshore Caspian "N Block." Secretary Rice raised this issue with Nazarbayev during her visit in October, and both she and Secretary Gutierrez wrote letters in support of CP's bid to

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President Nazarbayev in early February. CP tells us that their bid is fiscally and technically superior to Shell's, and CP has the added advantage of already having done extensive geophysical and geological work on the block. Securing CP a place in the Production Sharing Agreement (even if in partnership with Shell) would be a geopolitical as well as a commercial triumph: CP estimates N Block reserves a 2 billion barrels, and the field is expected to anchor future development in Kazakhstan's Southern Caspian region. Furthermore, the gas-rich field would be ideally located to supply gas to a future Trans-Caspian pipeline.

¶10. (C) We also ask for your assistance in resolving a long-standing legal case against Tom Dvorak, an American citizen executive of mid-sized PetroKazakhstan, Canadian company recently sold to China. The GOK has filed both criminal and civil charges against Dvorak for alleged violations of the anti-monopoly law. While we have not taken a position on Dvorak's guilt or innocence, we do feel that it is inappropriate for the Kazakhstani authorities to file criminal charges in what is a civil dispute. Dvorak recently applied to benefit from a December 2005 Amnesty Law; despite the fact that his case seems to fit under the terms of the Amnesty, his application and subsequent appeal have been denied. (Not for discussion with the GOK: We feel that Dvorak is likely being used as a pawn in ongoing negotiations

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between the GOK and the Chinese oil company over terms of the latter's October 2005 purchase of PetroKazakhstan.) If you get an opportunity with the President, it might be helpful if you were to suggest that, should Dvorak's case proceed to trial, the resulting coverage in the Western media might reduce investor enthusiasm for the Kazakhstani market.

Regional Infrastructure Integration

¶11. (C) During her October 2005 visit, Secretary Rice announced a new "Central Asia Infrastructure Initiative," with the objective of encouraging increased infrastructure (energy, transportation, communication) linkages between Central and South Asian countries. President Nazarbayev, in turn, has spoken favorably of Kazakhstan assuming a larger regional role, and during a recent conference on Afghanistan reconstruction, Foreign Minister Tokayev pledged Kazakhstan's assistance. In terms of energy initiatives, Kazakhstan is well-placed to trade electricity with its Central Asian neighbors. A 500 kV North-South transmission line currently being built in Kazakhstan could be used to transmit electricity from Kyrgyzstan and Tajikistan to Russia;

however, the GOK would have to grant access to its lines.

Non-Proliferation Issues

¶12. (C) Threat reduction and non-proliferation have been a cornerstone of the bilateral relationship since Kazakhstan's independence. Nazarbayev's 1991 decision to give up Kazakhstan's nuclear arsenal was groundbreaking. Kazakhstan returned all tactical nuclear warheads to Russia by January 1992, and all strategic nuclear warheads by April 1995. Through the Nunn-Lugar CTR program the U.S. assisted Kazakhstan with the destruction of bombers, missiles, and silos. Cooperation continues under the CTR program to secure the former Soviet nuclear weapons test site at Semipalatinsk.

Through the Biological Weapons Proliferation Prevention program, we are working with the GOK to combat bioterrorism and prevent the proliferation of biological weapons technology, pathogens and expertise. Under the recently signed Proliferation Prevention Initiative agreement (WMD-PPI), we will work with Kazakhstan to strengthen its ability to prevent proliferation of WMD and related materials across its borders by enhancing its WMD detection and interdiction capabilities along the Caspian Sea border.

¶13. (C) DOE's programs in Kazakhstan, including the decommissioning of the BN-350 reactor in Aktau; materials protection, control, and accountability assistance; and the proposed LEU conversion of the Alatau research reactor, of course represent a significant portion of our non-proliferation cooperation with Kazakhstan. While the latest BN-350 program review showed the project to be on schedule, contacts at the Ministry of Energy and Mineral Resources are prone to complain of delays and a lack of USG commitment to the full scope of the project. Your visit will be a valuable opportunity to update the GOK on the successful progress of the project and to reiterate the USG's support for the move of spent fuel to the Baykal-1 facility in Semipalatinsk.

¶14. (C) Post hopes that you will also use your meetings to push for conclusion of a Second Line of Defense (SLD) Implementing Arrangement. Negotiations with the GOK have dragged on for several years, apparently due to a lack of motivation on the GOK side. Although President Nazarbayev's positive response to you on SLD in Baku in May 2005 prompted an additional round of negotiations in September 2005, the GOK has not yet approved the resulting revised draft agreement. Contacts at the Ministry of Foreign Affairs and the Customs Control Committee have been saying informally for several months that there are no remaining substantive issues to be resolved with the draft agreement. Post hopes that your meetings will reveal whether there is political will within the GOK to conclude and implement an SLD agreement, or whether it is time to redirect the USG's limited resources elsewhere.

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